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IN THE MATTER OF:)

)

DETERMINATION OF RATES) Docket No.

AND TERMS FOR MAKING AND) 16-CRB-0003-PR

DISTRIBUTING PHONORECORDS) (2018-2022)

(PHONORECORDS III),)

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OPEN SESSION

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9 (PHONORECORDS III),)
10 -----X
11 BEFORE: THE HONORABLE SUZANNE BARNETT
12 THE HONORABLE JESSE M. FEDER
13 THE HONORABLE DAVID R. STRICKLER
14 Copyright Royalty Judges
15
16 Library of Congress
17 Madison Building
18 101 Independence Avenue, S.E.
19 Washington, D.C.
20
21 March 14, 2017
22 12:07 p.m.
23 VOLUME IV
24 Reported by:
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1 P R O C E E D I N G S

2 (12:07 p.m.)

3 JUDGE BARNETT: Good morning. Please be
4 seated. Are we all present and accounted for? Yes,
5 we are.

6 Mr. Marks, we're calling your witness
7 this morning?

8 MR. MARKS: Pandora calls
9 Michael Herring.

10 JUDGE BARNETT: Please raise your right
11 hand.
12 Whereupon--

13 MICHAEL HERRING,
14 having been first duly sworn, was examined and
15 testified as follows:

16 JUDGE BARNETT: Please be seated.

17 DIRECT EXAMINATION

18 BY MR. MARKS:

19 Q. Good morning, Mr. Herring. Would you
20 please state your full name for the record?

21 A. Michael Herring.

22 Q. Where do you work?

23 A. Pandora Media.

24 Q. How long have you worked at Pandora?

25 A. A little more than four years.

1 Q. What is your current job title?

2 A. President.

3 Q. How long have you served as president of
4 Pandora?

5 A. Just short of a year.

6 Q. Have you held any other positions at
7 Pandora during your tenure at the company?

8 A. I was formerly chief financial officer.

9 Q. Did Pandora recently hire a new chief
10 financial officer?

11 A. Yes.

12 Q. And when was that?

13 A. His first day was February 28th.

14 Q. Would you please explain what your job
15 responsibilities have been during your time at
16 Pandora and how, if at all, they are changing with a
17 new CFO onboard?

18 A. Well, as CFO, I was responsible for
19 overall financial management of the company,
20 including financial controls and reporting,
21 responsibility for investor relations, all our
22 systems, information systems, technology systems.
23 I, as president, took on more responsibility around
24 revenue. So that has been a change.

25 I've been also running our content

1 licensing programs for the last couple of years,
2 both related to statutory proceedings as -- as well
3 as our direct deal efforts with the music industry.
4 Lots of administrative responsibilities on top of
5 that, facilities, et cetera, but, you know, as --
6 now with the CFO, I focus almost exclusively on our
7 revenue businesses, so our advertising business, as
8 well as the launch and growth of our subscription
9 businesses, and then in conjunction with that, also
10 the -- the licensing, content licensing, side of our
11 cost structure.

12 Q. Did you prepare a written direct
13 testimony in connection with this proceeding?

14 A. Yes.

15 Q. If you could turn to the tab of the
16 witness binder in front of you marked as Pandora
17 Exhibit 880. Do you recognize this document?

18 A. 880. Yes.

19 Q. What is it?

20 A. It's my written direct testimony.

21 Q. If you could turn to the last page of the
22 document, please. Is that your signature?

23 A. It is.

24 MR. MARKS: I offer Pandora Exhibit 880
25 into evidence.

1 MS. BUCKLEY: No objection.

2 JUDGE BARNETT: 880 is admitted.

3 (Pandora Exhibit Number 880 was marked
4 and received into evidence.)

5 BY MR. MARKS:

6 Q. Did you also prepare written rebuttal
7 testimony in connection with this proceeding?

8 A. Yes.

9 Q. If you could turn to the tab that is
10 marked as Pandora Exhibit 888. Do you recognize
11 this document?

12 A. Yes.

13 Q. What is that?

14 A. It is my written rebuttal testimony.

15 Q. If you could please turn to the last
16 page. Is that your signature?

17 A. Yes.

18 MR. MARKS: I offer Pandora Exhibit 888
19 into evidence.

20 MS. BUCKLEY: No objection.

21 JUDGE BARNETT: 888 is admitted.

22 (Pandora Exhibit Number 888 was marked
23 and received into evidence.)

24 BY MR. MARKS:

25 Q. And, Mr. Herring, were both your direct

1 testimony and your -- your written direct testimony
2 and your written rebuttal testimony submitted before
3 Pandora hired a new chief financial officer?

4 A. That's correct.

5 Q. Have you prepared some slides to use in
6 connection with your live testimony today?

7 A. Yes.

8 Q. Could you go to the next slide, which is
9 titled Overview of Testimony. Broadly speaking, are
10 these the topics you're going to cover during your
11 testimony today?

12 A. Yes.

13 Q. Are all of these topics addressed in
14 additional detail in your written testimony?

15 A. Yes.

16 Q. The judges are generally familiar with
17 your -- excuse me, generally familiar with Pandora
18 from the Web IV proceeding and the testimony of your
19 colleagues, but could you just briefly walk the
20 judges through the history of the company?

21 A. Sure. So Pandora was founded by
22 Tim Westergren 17 years ago as Savage Beast. The
23 initial idea was to create the Music Genome Project
24 as a way of using technology to provide a music
25 recommendation engine. That initial incarnation was

1 focused on in-store applications. So inside a
2 BestBuy or a Tower Records, when people would go buy
3 CDs and -- and records in store, there would be a
4 kiosk where they could get recommendations for other
5 music, based on some music that they liked.

6 That business failed, and in 2004 Savage
7 Beast pivoted its business model to focus on
8 streaming radio and, specifically, personalized
9 radio, enabled by the Music Genome Project. And
10 Pandora was launched in 2005 and grew largely by
11 word of mouth. It was a very organic growth story
12 for a long time and -- and it -- you know, enabled,
13 by the rapid growth of connectivity. The
14 introduction of Smartphones, the introduction of the
15 iPhone in particular, was a major catalyst into the
16 adoption of Pandora as a -- as a music service.

17 And the company went public in 2011 and
18 grew to 80 million monthly active users, or MAUs, by
19 2014, where it has been relatively flat since then,
20 hovering around 80 million monthly active users.

21 In 2015, we started the development of
22 interactive product offerings, so kind of next
23 generation music services. Pandora has always been
24 a non-interactive radio service, both ad-supported
25 and subscription. And we started working on the

1 licensing side of it with the music industry, as
2 well as the technology, including acquiring the
3 assets of a bankrupt competitor called Rdio in the
4 fall of 2015 to accelerate those efforts.

5 In 2016, we completed the licensing to
6 launch the new -- new services. We, you know,
7 redesigned the service. We launched a new brand.
8 And we launched the first of two subscription
9 products, the Pandora Plus, which replaced Pandora
10 1, which was the ad-free version of the
11 non-interactive service and which added new
12 functionality.

13 And we are launching tomorrow Pandora
14 Premium, which is our full interactive on-demand
15 service.

16 Q. Mr. Herring, how would you describe
17 Pandora's mission?

18 A. Our mission is -- is, at a high level,
19 twofold. One is -- is to connect users, listeners
20 with the music that they love and help them discover
21 new music, and on the other side of it, to help
22 artists, musicians find the audiences they deserve
23 by exposing their music to new audiences, by
24 streaming their music to their fans and -- and
25 providing revenue streams back to those artists.

1 Q. And has that been Pandora's mission
2 throughout its existence?

3 A. It has.

4 Q. If you would please turn to the tab
5 marked as Pandora 881 in your binder. Do you
6 recognize this document?

7 A. I do.

8 Q. What is it?

9 A. This is a presentation we prepared in
10 conjunction with an investor analyst day we did in
11 the fall of last year. It walks through our
12 strategy, our product strategy around the launch of
13 new services, as well as the financial model
14 underlying our business strategy.

15 Q. Did you personally participate in the
16 preparation of this document?

17 A. Yes.

18 Q. Was this document appended to your
19 written direct testimony as an exhibit?

20 A. Yes.

21 MR. MARKS: I offer Pandora Exhibit 881
22 into evidence.

23 MS. BUCKLEY: No objection.

24 JUDGE BARNETT: 881 is admitted.

25 (Pandora Exhibit Number 881 was marked

1 and received into evidence.)

2 BY MR. MARKS:

3 Q. I'd like to turn now to Pandora's
4 investments in innovation and product development
5 and ask you to describe a few examples.

6 A. So over the last 17 years, we've made a
7 lot of investments in innovation and product, and it
8 has come a long way. It's critical for our ability
9 to grow our business and serve our listeners as well
10 as possible.

11 You know, I've already mentioned the
12 Music Genome Project. That's kind of the central
13 original investment. The Music Genome Project is an
14 effort where musicologists or musicians listen to
15 millions of songs or have over the last 17 years and
16 -- and scored those songs across as many as 450
17 attributes, everything from tone and tempo to genre,
18 to, you know, the -- the instruments involved to the
19 -- the voice and the style of the voice, et cetera,
20 to create a number stream that represents sort of
21 the music genomic equivalent of that song.

22 And then we can compare that to other
23 streams for other songs in order to calculate a
24 mathematical approximate, how close those songs are.
25 And in order to then -- if one song is close to

1 another and you like one song, the chances that
2 you'll like that next song are higher. And so it's
3 something that -- an approach to music
4 recommendations that's unique to Pandora, something
5 that's -- we've spent a lot of time and money,
6 obviously, investing in.

7 Algorithms lay on top of that. These are
8 our data science team uses math to take data like
9 the Music Genome Project, like the massive amounts
10 of thumb data that Pandora has, over 80 billion
11 thumbs over the last ten years. That's interactions
12 with consumers telling us that they like a song or
13 don't like a song in the context of a station.

14 JUDGE BARNETT: By thumbs, you mean
15 thumbs up/thumbs down?

16 THE WITNESS: Thumbs up and thumbs down.
17 So, actually, in the interface of the project,
18 there's a little thumb up and a thumb down icon.
19 You don't have to touch anything, but if you give
20 that feedback, it will -- we will incorporate that
21 into -- into the play listing, how we program the --
22 the station for you.

23 That's something that is very core to our
24 IP as a company.

25 JUDGE STRICKLER: Is your thumbs

1 up/thumbs down feature going to be or is it part of
2 the interactive features?

3 THE WITNESS: Well, so in the interactive
4 products, there's the radio function, is absolutely
5 important to the overall music experience for a
6 bunch of reasons. Most of the listening will still
7 be non-interactive, even in those products.

8 And we estimate north of 70 percent of
9 listening, even in an interactive product, is
10 non-interactive listening or listening to radio
11 stations or playlists, but the way the thumbs work
12 is a lot of the interactive features are influenced
13 by the data that's in the thumbs.

14 And so, you know, for example, a playlist
15 builder, what we choose to build that playlist for
16 you, the songs we choose is -- is influenced heavily
17 by the thumbs that have been contributed to the
18 service.

19 JUDGE STRICKLER: So you're saying the --
20 the investment that was made in the technology that
21 allows for a thumbs up/thumbs down incorporation
22 into your algorithm, that investment is usable in
23 the interactive space as well?

24 THE WITNESS: It's actually -- it's very
25 usable. In fact, it's critical to our competitive

1 differentiation in the marketplace, actually. The
2 -- the interactive features that were -- might have
3 a similar feature set among competitors. Ours would
4 be unique in the sense that it would be personalized
5 to the listener because of the data we have around
6 thumb activity that comes from the radio service.

7 JUDGE STRICKLER: When the -- when the
8 investments were made in these thumbs up/thumbs down
9 algorithms or, even more broadly, in the -- in the
10 technology that developed the non-interactive
11 product, was there an intentional -- more
12 importantly, will the record reflect from your
13 testimony or the testimony of anyone else at Pandora
14 that the investments were made with the intention of
15 expanding them into the interactive space at some
16 future period of time?

17 THE WITNESS: Well, I can't speak to 17
18 years ago. I've been at the company four years.

19 JUDGE STRICKLER: Do you have any
20 institutional knowledge?

21 THE WITNESS: Yeah, well --

22 JUDGE STRICKLER: And, again, I'm really
23 asking about whether it's -- whether it's in your --
24 your testimony or the testimony of anyone else in
25 this proceeding, rather than asking you to go beyond

1 anything that -- the testimony.

2 THE WITNESS: Yeah. I mean, my testimony
3 is that the investment we made in the
4 non-interactive project and specifically the Music
5 Genome Project, the algorithms that lay on top of
6 that, the service that collects the 80 billion
7 thumbs, the math that uses those thumbs to customize
8 and personalize the experience are all critical to
9 the development of the products that we're bringing
10 to market.

11 So there's two subscriptions. The Plus
12 subscription is -- is not an on-demand subscription.
13 It's all radio. So it's absolutely critical to that
14 product.

15 From a Premium -- the Premium product,
16 which has on-demand, you can listen to an album or
17 build your own playlist song by song, those
18 features -- we are laying new features on top of
19 that, that are enabled by the investments we made
20 previously. So, you know, I would argue that
21 whether it was contemplated that that specific
22 product would be the outcome, I wouldn't say that
23 that's true. I would say back when we were
24 developing the strategy for entering the market, the
25 -- the reason we decided to do so is because we

1 believed we could be competitive because we had this
2 data asset.

3 JUDGE STRICKLER: Is it your
4 understanding that the Pandora Plus, which is the --
5 the mid-range, if you will, if you'll allow me,
6 mid-range product.

7 THE WITNESS: Yep, mid-range is accurate.

8 JUDGE STRICKLER: That that will pay --
9 that recordings or -- there will trigger the payment
10 of a mechanical license? The playing of -- of songs
11 on Pandora Plus will trigger payments on -- under
12 the mechanical license or only Pandora Premium?

13 THE WITNESS: No, both Plus and Premium.

14 JUDGE STRICKLER: You described Plus as
15 basically a non-interactive radio. Is it because of
16 the replays of the other features that --

17 THE WITNESS: Replays, off-line
18 listening, et cetera, yes.

19 JUDGE STRICKLER: Thank you.

20 BY MR. MARKS:

21 Q. Mr. Herring, what are the qualifications
22 and expertise of the employees involved in the music
23 genome coding -- project coding process?

24 A. So employees that we hire for that
25 project are all musicians, musicologists. They've

1 studied music theory, music composition. They go
2 through a very rigorous testing program before even
3 being offered the job. So there's a very high bar
4 to get over. Once they've been -- they've passed
5 that, then they go through additional training to
6 learn the Pandora way of analyzing music.

7 If -- you know, if you think about 17
8 years and dozens and dozens of music analysts, in
9 order for an algorithm to work effectively, it has
10 to be a very consistent analysis, scoring across --
11 across millions of songs in order for a song that
12 was analyzed ten years ago to be comparable to a
13 song that was analyzed yesterday.

14 And so that -- there's not only a lot of
15 training about how we do it the Pandora way, but
16 quality assurance that goes both ways. So we -- you
17 know, we consider them as expert in their -- in
18 genres or in music theory and composition as -- as
19 anybody.

20 Q. What sort of investment of time has been
21 associated with creating and refining the Music
22 Genome Project over the years?

23 A. Well, each song takes 20 minutes to an
24 hour for a, you know, classical composition to -- to
25 analyze. We -- we've analyzed millions of songs at

1 this point. I would say the number of hours of
2 human time to do that is definitely hundreds of
3 thousands of hours.

4 Q. And are you able to quantify the expenses
5 associated with creating and refining the Music
6 Genome Project?

7 A. Well, you know, that part -- it's 17
8 years of not just the time and effort of those
9 people, but the -- the engineers who developed the
10 technology in order to enable that data to deliver a
11 service, you know, in -- in excess of 200 million
12 dollars over that time frame.

13 Q. And if you hadn't already built the music
14 -- hadn't already started building the Music Genome
15 Project in connection with the non-interactive
16 ad-supported tier service and wanted to just start
17 from scratch for Pandora Plus and Pandora Premium,
18 would you need to build something like the Music
19 Genome Project?

20 MS. BUCKLEY: Objection, calls for
21 speculation.

22 JUDGE BARNETT: Sustained.

23 BY MR. MARKS:

24 Q. Just so the record is clear, I'm not sure
25 if it came out; I apologize if I'm asking you

1 something that you've covered in part before. Do
2 Pandora's interactive products rely on the Music
3 Genome Project?

4 A. Yes.

5 Q. Do the algorithms that you mentioned a
6 moment ago, do the algorithms that Pandora has
7 developed allow Pandora to bring new features to the
8 interactive marketplace that are not available from
9 any other service?

10 A. Yes.

11 Q. How do they do that and what are some of
12 those features?

13 A. Well, so I mentioned earlier the playlist
14 builder. One of the big problems with interactive
15 services or playlist building in general is most
16 people -- and we know this from acquiring the assets
17 in 100, nearly 100 people out of the -- the
18 bankruptcy of Rdio, a failed service, beloved by
19 its, unfortunately for them few users, but -- but a
20 failed service that spent hundreds of millions of
21 dollars and didn't survive -- was that people would
22 start playlists with enthusiasm, get three or four
23 songs in, and run out of steam.

24 And those were called orphaned playlists.

25 MS. BUCKLEY: Objection, beyond the scope

1 of written direct testimony.

2 JUDGE BARNETT: I don't think so.

3 MR. MARKS: I don't think it is. I can
4 find the paragraph cite.

5 JUDGE STRICKLER: I don't know that he
6 testified specifically, you'll check it out, about
7 -- the general point, yes, but I don't know if it
8 was related to Rdio per se. It might be just a
9 little more detail, but I could be wrong, so if you
10 could point to where he -- where he links up the
11 behavior of Rdio customers.

12 MR. MARKS: Well, if you -- if you just
13 look at, for instance, paragraph 22 and 23 and 24 of
14 his -- his written direct testimony, there's
15 extensive discussion of how the algorithms are used
16 in connection with product features that would be
17 part of the interactive services.

18 JUDGE STRICKLER: It was the extra detail
19 about comparing Rdio's listeners to -- to listeners
20 on Pandora that I think -- and, again, maybe I'm
21 wrong. Maybe you can point to a section where --
22 because the objection is it's beyond the scope of
23 his written direct. And I -- is that the -- is that
24 the nature of your objection?

25 MS. BUCKLEY: That is one thing, but also

1 there is no discussion of playlists or orphaned
2 playlists, as far as I can tell, in the written
3 direct statement.

4 JUDGE STRICKLER: Well, I think it does
5 talk about playlists. He just -- I don't know that
6 he uses the phrase "orphaned playlists," but he
7 describes something and he -- now he's just giving
8 it a name. So I don't know that that necessarily
9 goes beyond the scope of his direct by naming
10 something that's already in there.

11 JUDGE BARNETT: I reviewed it this
12 morning. I know "orphaned playlist" is in this
13 paper. So overruled.

14 MR. MARKS: Thank you, Your Honor.

15 THE WITNESS: So the -- the context of
16 using that example is that one of the challenges of
17 -- of building playlists and engaging users in an
18 interactive service is where do they go after their
19 initial idea for a playlist, the first three or four
20 songs?

21 What Pandora does extremely well is take
22 a seed, a song, song titles in this case, and using
23 the data underlying that user's musical preferences,
24 suggests another song and another song and another
25 song. And so the add -- add new similar songs

1 feature within the interactive feature, the playlist
2 builder, is driven by the Music Genome Project, the
3 thumb data from non-interactive services with
4 algorithms laid on top of it in order to enable that
5 feature.

6 And it's one of the -- the hallmarks of
7 the Premium product that's coming out tomorrow.

8 BY MR. MARKS:

9 Q. In addition to all of the work Pandora
10 has done to build its service, has Pandora made
11 investments to make it easier for consumers to
12 access the service?

13 A. Yes. We've made significant investments
14 in order to make sure that people can listen to
15 Pandora however they choose to do so. It started
16 out as a desktop app. We made significant
17 investments in order to have Pandora work
18 effectively on Smartphones. And a lot of our growth
19 early on was based upon the popularity of iPhone,
20 iOS and Android devices.

21 We've invested a lot of time, money, and
22 effort into integrating into automobiles. We've had
23 over 25 million integrations activated within cars
24 in the United States. Over half of all models that
25 will be sold in 2017 will have Pandora integrated

1 into the dash. That takes a lot of time and effort
2 from a technological perspective to work with dozens
3 of auto provides on that front.

4 And CE devices as well, so consumer
5 electronics devices, like everything from smart TVs
6 to home entertainment systems like Sonos, Roku,
7 Apple TV, xfinity cable boxes, Amazon Echo, Google
8 Home, are all -- we have invested a lot of money and
9 effort to make sure that Pandora is integrated into
10 those systems and works really easily and
11 effectively, so as people want to listen to Pandora,
12 they can listen to it on their phone. If they get
13 home, they can switch it onto their home
14 entertainment device. They can listen to it in the
15 car as they're driving to work. So that
16 accessibility to our service is a hallmark of -- of
17 our strategy.

18 JUDGE BARNETT: Mr. Herring, I don't
19 think my refrigerator has Pandora. You mentioned
20 refrigerators in your testimony.

21 THE WITNESS: There is a refrigerator and
22 hot tub that has Pandora integrated into the
23 control.

24 BY MR. MARKS:

25 Q. Switch to the cameras.

1 A. Microwaves, I have not seen -- I have not
2 seen a microwave with Pandora in it. Yeah, that's
3 -- you know, that speaks actually to the -- the
4 reason we've been able -- we don't pay for any of
5 these integrations. So there's no fees back to --
6 to have us integrated.

7 These are brands that come to Pandora to
8 have Pandora integrated as a feature to market
9 themselves. Even the Amazon Echo is a great example
10 of that, where obviously they have their own music
11 service, but on the box for the Echo, it advertises
12 integrate seamlessly into your Pandora account.
13 That's because having Pandora drives engagement,
14 which is what the Echo is really trying to do with
15 their customers.

16 JUDGE BARNETT: Does that include
17 automobiles? You're not paying for integration?

18 THE WITNESS: We don't pay for any
19 integration there. It's different model than Sirius
20 has. They pay or have historically paid for
21 integration.

22 JUDGE BARNETT: Thank you.

23 BY MR. MARKS:

24 Q. What is the order of magnitude of the
25 investments Pandora has made to facilitate expanded

1 consumer access to its service?

2 A. Well, on the accessibility side,
3 certainly tens of millions of dollars over the
4 years.

5 Q. What role did Pandora play in building a
6 market for Internet radio advertising?

7 A. Well, I mean, you know, I think we,
8 because we were first, really created that market.
9 We had to build it from scratch.

10 Q. And are the efforts and investments
11 associated with building that market described in
12 your written direct testimony?

13 A. Yes.

14 Q. And why was it important to Pandora to
15 create a market for Internet radio advertising?

16 A. Well, our non-interactive service, which
17 is free to the consumer, has significant royalty
18 costs that we needed to cover. And so we needed to
19 find ways to monetize it.

20 And advertising was the most readily
21 available.

22 Q. Will -- will Pandora be offering an
23 ad-supported interactive service or does it have
24 plans to offer an ad-supported interactive service?

25 A. No.

1 Q. Why is the investment Pandora makes in
2 growing the market for Internet advertising
3 important to the development of Pandora's
4 interactive subscription products?

5 A. So our approach to driving subscription
6 products is to build an audience, the largest
7 audience possible, in the free-to-the-consumer
8 ad-supported business and then upsell and cross-sell
9 those users by offering value propositions, like
10 off-line listening for Plus or like on-demand
11 features and functionality for Premium, into those
12 services.

13 You know, there are other ways of
14 aggregating users and converting them into
15 subscription. You can just acquire -- you know, pay
16 for them through search or through advertising. We
17 choose to -- we think it's a better model to
18 aggregate them by providing a high-quality
19 ad-supported service and then upsell, cross-sell
20 them from there, because the ad-supported business
21 generates revenue and -- and contribution margins
22 itself.

23 So the investment we've made to grow that
24 business creates the pool of users that we will draw
25 from in order to build our subscription business.

1 Q. If you could turn to the tab in your
2 binder that's marked as Pandora Exhibit 891. Do you
3 recognize that document?

4 A. I do.

5 Q. What is it?

6 A. This is a graph showing the progress over
7 the last three years of the hours or -- the hours of
8 music consumed by listeners on our service, as well
9 as the revenue per thousand hours that we have been
10 generating off of advertising on that service.

11 JUDGE FEDER: Excuse me, Mr. Herring. Is
12 that what RPM stands for?

13 THE WITNESS: Yes, revenue per thousand
14 hours.

15 JUDGE FEDER: Thank you.

16 BY MR. MARKS:

17 Q. Was this document appended to your
18 written rebuttal testimony as an exhibit?

19 A. Yes.

20 MR. MARKS: I offer Pandora Exhibit 891
21 into evidence.

22 MS. BUCKLEY: No objection.

23 JUDGE BARNETT: 891 is admitted.

24 (Pandora Exhibit Number 891 was marked
25 and received into evidence.)

1 BY MR. MARKS:

2 Q. Mr. Herring, what does Pandora's dynamic
3 insertion technology do?

4 A. That technology was developed to, based
5 upon listening behavior, determine the right moment
6 to interrupt the music listening stream.

7 Q. And is that the same thing as what's
8 referred to in some Pandora documents as intelligent
9 interruptions?

10 A. It is, yes.

11 Q. Does Pandora use this technology for
12 anything in addition to delivering advertising?

13 A. Well, it was developed primarily to drive
14 advertising. It is used for anything that's going
15 to interrupt the music experience. So, initially,
16 that was advertising, when to -- when to play an ad
17 in order to make it most effective, but also least
18 disruptive to the music listening experience.

19 We use it as well for artist audio
20 messages, live events, promotions, any -- any sort
21 of interruption to the music that -- or any
22 interruption to the playing of music that is a
23 non-music use.

24 Q. What are the benefits of artist messaging
25 on Pandora for artists and fans?

1 A. Well, start with fans. I mean, our
2 research and experience now, having served millions
3 of these messages, is that fans like the connection
4 to the artist. They like to hear their -- the voice
5 -- the artist. They like to find out about new
6 releases and events coming up, so they look at it
7 very much as a value add to the experience.

8 One of the fears was they would look at
9 it as an advertisement, and so we did a lot of
10 testing and actually the -- that -- by inserting
11 artist audio messages, listeners on average listened
12 longer and come back more. So it had an aura effect
13 to the overall service. From an artist -- recording
14 artist perspective, they've used it for all kinds of
15 ways.

16 What we did is created a tool that let
17 the creatives be creative. And so it's everything
18 from thanking fans from listening to their station,
19 to introducing a new song that's being released, to
20 promoting an album, to promoting live events or
21 concerts with links to the tickets. You know, we've
22 seen a lot of very interesting ways of doing it.

23 That benefit has, you know, done
24 everything from sell -- sell tickets to drive
25 listening of new music, help -- help them chart,

1 help them get exposure to new music, spin their
2 music more, and certainly has driven attendance to
3 concerts.

4 Q. How do songwriters and music publishers
5 benefit from artist messaging on Pandora?

6 A. Well, to the -- you know, to the extent
7 that songwriters are also the -- the performing
8 artist, they benefit from -- from that exposure as
9 well, the songwriter. To the extent it drives more
10 listening or exposes their music, they benefit from
11 the royalties associated with that. To the -- both
12 publishers and songwriters would benefit from those
13 additional royalties.

14 To the extent it drives people to live
15 events, the songwriters and publishers benefit from
16 the royalties they receive through the performing --
17 performance rights that venues pay -- pay around
18 live events.

19 Q. What is Pandora's artist marketing
20 platform?

21 A. Artist marketing platform, or AMP, is --
22 it's a dashboard. It's a -- that artists can claim
23 their identity and log in and view all their
24 listening data on Pandora, as well as access
25 marketing tools, one of which is the artist audio

1 message.

2 Q. What sort of decisions does the artist
3 marketing platform help artists to make?

4 A. Well, data is powerful. It's -- you
5 know, it's the new oil, right, as someone just said
6 recently. So for artists, performing artists, in
7 particular, they can look to see what songs are --
8 are trending, how they're trending up or down and by
9 location as well. So, you know, they can -- as
10 they're going to a city to perform, they can look
11 and see what songs are popular in that city and --
12 and adjust their set list accordingly.

13 They can look at what songs are
14 performing well, being thumbed up or thumbed down,
15 in order to put their own marketing efforts behind
16 those that are trending more positively than others.
17 They can look at demographics across the U.S. and
18 look for pockets of their audience where there's
19 concentrations and plan tours accordingly. So
20 there's lots of -- lots of benefits to recording
21 artists based upon the -- the data in AMP.

22 Q. And do songwriters and music publishers
23 benefit from AMP?

24 A. Well, once again, to the extent the
25 songwriter and the recording artist are the same,

1 they benefit in all those ways. But, you know, I
2 think I already kind of highlighted what they
3 benefitted from is -- is if they have exposure drive
4 additional listening to their music, there's
5 additional royalties associated with that. If it
6 drives more activity in the -- in the touring
7 aspect, they'll benefit from their music being
8 played at live events, et cetera.

9 Q. If you could turn to the tab in your
10 binder that's marked as Pandora Exhibit 882. Do you
11 recognize this document?

12 A. Yes.

13 Q. What is it?

14 A. This is a description of AMPcast and
15 artist audio messaging and AMP generally that is
16 available on our web site for artists to go learn
17 about the services.

18 Q. Was this document appended to your
19 written direct testimony as an exhibit?

20 A. Yes.

21 MR. MARKS: I offer Pandora Exhibit 882
22 into evidence.

23 MS. BUCKLEY: No objection.

24 JUDGE BARNETT: 882 is admitted.

25 (Pandora Exhibit Number 882 was marked

1 and received into evidence.)

2 BY MR. MARKS:

3 Q. Mr. Herring, were additional investments
4 required to develop the interactive features of
5 Pandora Plus and Pandora Premium?

6 A. Yes.

7 Q. Are those investments described in -- in
8 detail in your written direct testimony?

9 A. Yes.

10 Q. Has Pandora invested over 100 million
11 dollars in this initial launch?

12 A. Yes.

13 JUDGE STRICKLER: Question for you,
14 Mr. Herring, with regard to these additional
15 investments. When the investments are made, are
16 they made out of -- by outside third-party
17 investors, are they done out of the internal capital
18 accumulated by Pandora, or some -- or a combination?

19 THE WITNESS: So, explicitly, they've
20 been made out of our internal capital. So the
21 capital that -- that we generate from our
22 non-interactive advertising business, for example,
23 has been reinvested aggressively and --

24 JUDGE STRICKLER: Retained earnings,
25 basically?

1 THE WITNESS: Yes. So that -- in 2016,
2 that happened, that was a pretty significant shift
3 in investment to -- to build the interactive
4 services and get the services Plus launched in the
5 fall and Premium launched tomorrow.

6 JUDGE STRICKLER: Does it also come out
7 of public and/or private placements or public
8 offerings or anything else?

9 THE WITNESS: Yeah, I'd -- we've -- we've
10 also drawn down significantly on the capital
11 accounts in our balance sheet, which we have raised
12 money, first in the IPO, and then we did a secondary
13 equity offering two and a half, three and a half
14 years ago, and then a convertible debt offering a
15 year and a half ago in order to add cash to the
16 balance sheet which we subsequently invested.

17 JUDGE STRICKLER: I was going to ask you
18 about debt financing. Is it only just convertible
19 debt financing or is there just straight financing
20 as well?

21 THE WITNESS: We also have an
22 asset-backed line that we use to manage cash flows.

23 JUDGE STRICKLER: An asset-backed line of
24 credit?

25 THE WITNESS: Line of credit, yes.

1 JUDGE STRICKLER: And when you -- when
2 the investments are done internally out of retained
3 earnings or out of the capital account of Pandora,
4 do you make a decision as to whether or not the --
5 the investment is worthwhile given a range of
6 potential royalties across the royalty board? Does
7 that come into your -- your analysis; that is, do
8 you say, well, this -- we will get -- we believe
9 we'll have a net profitable return on this
10 investment, given the royalty rate structure that
11 exists, but if the royalties change, and you do some
12 sort of a sensitivity analysis as to whether or not
13 the investment is worth it based on different
14 royalty structures?

15 THE WITNESS: So, yes, we do -- we do
16 evaluate the stability of royalty structures, maybe
17 is the best way of putting that. Certainly, that's
18 a risk. These are not fixed inputs. You know,
19 whether it's every five years here through this
20 proceeding or other proceedings or it's every two or
21 three years in direct deals, you know, those rates
22 become negotiable.

23 So we look at things like industry trends
24 and practice, you know, to get some sense of what we
25 believe are sustainable royalty rates and then --

1 and base our ROI calculations on that.

2 JUDGE STRICKLER: Do you know if there's
3 any evidence in the record that -- that Pandora has
4 produced that sets forth a sort of a sensitivity
5 analysis as to what the rate of return might be with
6 regard to different investments given different rate
7 structures?

8 THE WITNESS: Well, I know we've done
9 direct comparisons between the proposals in front
10 today, and that's in the record. And -- but in
11 terms of overall sensitivities, I'm not sure that --
12 that that has been presented.

13 JUDGE STRICKLER: I know you've -- you've
14 included in your testimony something that I would
15 call sort of descriptive --

16 THE WITNESS: Yes.

17 JUDGE STRICKLER: -- of the ramifications
18 if the Copyright Owners' royalty structure were to
19 -- were to be adopted. Is there anything more
20 granular than that or is that what you're referring
21 to when you say you've already placed in the record
22 information, evidence with regard to the impact of
23 -- of different rate structures?

24 THE WITNESS: No, there's a -- there's an
25 analysis that I did for my Board that compares the

1 royalty structure of our proposal versus the NMPA
2 proposal.

3 JUDGE STRICKLER: Is that attached as an
4 exhibit or otherwise explained or described in the
5 testimony of any of the Pandora witnesses?

6 THE WITNESS: Yes. I think it's --

7 MR. MARKS: I'm not sure.

8 THE WITNESS: I'm not sure, actually,
9 yeah. I don't know.

10 MR. MARKS: He will be testifying about
11 the analysis that was done in comparing the rate
12 proposals later in today's examination.

13 THE WITNESS: Yeah.

14 BY MR. MARKS:

15 Q. Has Pandora achieved profitability in any
16 year since becoming a public company?

17 A. No.

18 Q. What is the principal obstacle to
19 Pandora's ability to achieving sustained
20 profitability?

21 A. It has been high content royalty costs.

22 Q. In deciding to enter the market for
23 interactive streaming, what assumptions did Pandora
24 make about the music publishing royalties it would
25 have to pay?

1 A. We made assumptions that they would stay
2 stable at where they are today.

3 Q. Why did you make that assumption?

4 A. Well, when we looked at what historical
5 precedent had been, they had stayed relatively
6 stable for a long -- for a long time, and -- and we
7 had done deals, direct deals, with our industry
8 partners at those rates.

9 Q. If you could turn to the tab that's
10 marked as Pandora Exhibit 890. Do you recognize
11 this document?

12 A. Yes.

13 Q. What is it?

14 A. This is a forecast through 2022 of the --
15 both the Plus, which is the tier 2 subscription, and
16 the Premium, which is the tier 3 subscription. You
17 know, our forecast for those revenue lines and their
18 relative profitability.

19 JUDGE STRICKLER: One of the lines there
20 is, Mr. Herring, total cost of revenue. Does --
21 does that -- that a royalty cost or does it include
22 royalty cost?

23 THE WITNESS: Well, total cost of royalty
24 revenue is both.

25 JUDGE STRICKLER: Both what? I'm sorry.

1 THE WITNESS: Cost of revenue-content
2 acquisition is the royalty cost.

3 JUDGE STRICKLER: Right.

4 THE WITNESS: The other is the cost of
5 streaming the service, the bandwidth, that sort of
6 thing.

7 JUDGE STRICKLER: So let's go to the line
8 item cost of revenue content acquisition. That's
9 the royalty line, right?

10 THE WITNESS: That's correct.

11 JUDGE STRICKLER: And is that based on a
12 particular assumption as to royalties?

13 THE WITNESS: Yes, it's based on a series
14 of assumptions, yes.

15 JUDGE STRICKLER: And not just a
16 mechanical royalty but performance royalties and
17 sound recording royalties; that's everything?

18 THE WITNESS: That's correct. That's all
19 of it lumped together.

20 JUDGE STRICKLER: And it's the -- is it
21 the same going through from fiscal year '15
22 projected out to fiscal year 2022, the same rates --
23 same rates and same rate structures, if you know?

24 THE WITNESS: It's the rate structures
25 from a sound recording perspective as we've

1 negotiated in our direct deals, and it's a rate
2 structure, a publishing rate structure based upon
3 our proposals in this proceeding.

4 BY MR. MARKS:

5 Q. Is it based on Pandora's rate proposal or
6 was this based on the current rates and terms?

7 A. This one is based on -- well, it's
8 essentially the same rate. So I think this is based
9 on the current rates and terms.

10 MR. MARKS: I offer Pandora Exhibit 890
11 into evidence.

12 MS. BUCKLEY: I object to the entry of
13 this document as evidence. It lacks any evidentiary
14 support attached to see what the assumptions are and
15 how these numbers were derived.

16 JUDGE BARNETT: Yes, Mr. Marks, can you
17 lay a little foundation on this document?

18 MR. MARKS: Sure.

19 BY MR. MARKS:

20 Q. Mr. Herring, was -- was this -- was this
21 document prepared at your direction and under your
22 supervision?

23 A. Yes.

24 Q. And what -- what were -- what
25 assumptions, if any, changed over the period of time

1 reflected in Pandora Exhibit 890?

2 A. Well, so we moved into a direct licensing
3 environment, beginning in late 2016. So, hence,
4 there's a pretty dramatic change in our content cost
5 associated with -- obviously, going from '15 to '16,
6 there's also the impact of the CRB rate from a sound
7 recording perspective. In September of 2016, we
8 signed direct deals with the labels, which changed
9 our cost structure both for non-interactive -- both
10 for all three tiers, essentially, of service,
11 ad-supported, free-to-the-consumer tier, as well as
12 two subscription tiers.

13 And so those assumptions, while -- those
14 deals don't cover this entire time period. Those
15 assumptions are assumed to stay the same from a rate
16 perspective through this time period.

17 Q. And is this the type of analysis that
18 would -- that's typical of the analysis that Pandora
19 does in making business decisions?

20 A. Yes.

21 MR. MARKS: I offer Pandora Exhibit 890.

22 MS. BUCKLEY: I maintain my objection.

23 JUDGE BARNETT: Overruled.

24 MS. BUCKLEY: I still don't see any
25 underlying data that would support any of these

1 numbers.

2 JUDGE BARNETT: We'll allow it.

3 (Pandora Exhibit Number 890 was marked
4 and received into evidence.)

5 JUDGE STRICKLER: I have a question about
6 it, especially since now that it's in evidence.
7 Towards the bottom of -- of Exhibit -- Pandora
8 Exhibit 890, the fifth line from the bottom, there's
9 a line that says less INCR, which I'll -- which I
10 guess means increase. Is that right? Do you see
11 all the way to the left?

12 THE WITNESS: Yes.

13 JUDGE STRICKLER: Is that less increase
14 NMPA cost?

15 THE WITNESS: Yes.

16 JUDGE STRICKLER: And does NMPA in this
17 context stand for National Music Publishers
18 Association?

19 THE WITNESS: Yes.

20 JUDGE STRICKLER: What is that line
21 telling us?

22 THE WITNESS: It's telling us the
23 difference between the existing model and if it was
24 under the NMPA proposal.

25 JUDGE STRICKLER: Okay. So this actually

1 is sort of an elaboration on the answer you gave to
2 counsel's question before. The assumption
3 throughout this document is not your existing rate
4 structure and the -- the existing rate structure,
5 your proposed structure. This one line then builds
6 in an alternative, which is the NMPA structure?

7 THE WITNESS: Yes.

8 JUDGE STRICKLER: If that was to be
9 adopted by the judges?

10 THE WITNESS: Yes. We've done a full
11 analysis of it, but that's -- it is to summarize it
12 on a page, yes.

13 BY MR. MARKS:

14 Q. Mr. Herring, are you familiar with
15 Pandora's rate proposal in this proceeding?

16 A. Yes.

17 Q. Let me show you the slide summarizing
18 Pandora's rate proposal that we showed to the judges
19 during opening arguments. Why is Pandora proposing
20 to preserve the all-in rate structure with a
21 headline rate that covers both mechanical rights and
22 performance rights?

23 A. Well, for us, mechanical rights aren't --
24 aren't usable without the performance rights. We
25 look at it as a publishing rate. And so an all-in

1 rate allows us to operate the business with
2 certainty and -- and predictability.

3 Q. Why does Pandora favor a headline royalty
4 rate based on a percentage of revenues for its
5 interactive products?

6 A. In the context of subscription products,
7 in particular, where there's a fixed revenue per
8 user per month, a percentage of revenue is by far
9 the most rational way to structure a royalty payment
10 in the context that it allows for a connection
11 between our largest expense, which is royalty
12 expense, and the -- and the revenue associated with
13 it. So they move together.

14 If they didn't move together, that would
15 add uncertainty and volatility to our ability to run
16 the business.

17 Q. Why is Pandora proposing to preserve the
18 current headline rate of 10 and a half percent of
19 revenues?

20 A. Well, I mean, in all honesty, a lower
21 rate would be better for us and probably better for
22 the industry generally. It would allow us to have
23 more cash to reinvest in the business and grow the
24 business. Subscription business, in particular, are
25 all about, you know, growing to the maximum size

1 that the profits allow you to grow to.

2 The -- the less profitable a
3 subscription, the -- the smaller the subscription
4 business is going to be. That said, 10 and a
5 half percent is a rate that in our models, as you
6 can see, we believe we can build a business over
7 time. It's one that has, you know, been adopted
8 broadly in the industry and one that I feel has --
9 has worked so far.

10 So, rather than fight for a lower rate,
11 we figured keeping the status quo in a rate that we
12 could at least model out a profitable business over
13 time, it hasn't been proven yet by anybody that I'm
14 aware of, but over time, we believe we could model
15 out a profitable business here based on that rate.

16 BY MR. MARKS:

17 Q. Has Pandora proposed any change to the
18 royalty minimums in step 2 of the current
19 regulations?

20 A. No.

21 Q. Why has Pandora proposed to preserve the
22 variety of different rate categories from the
23 current regulations?

24 A. Well, I actually think that's really
25 important for the industry and for all parties

1 considered. I mean, having a diverse set of
2 offerings so that you can address multiple consumer
3 preferences is how we optimize a marketplace here.

4 You know, having one -- one price, one
5 price is going to suboptimize the environment.
6 There are people who would pay \$4.99 but wouldn't
7 pay \$9.99. If you don't have an offering at the
8 \$4.99 level, those -- it's not, those people don't
9 pay \$9.99. They choose other offerings. Whether
10 it's free offerings or piracy or whatever, it would
11 -- has been historically.

12 So I think having multiple tiers allows
13 for innovation. It allows for diversity from a
14 product perspective. And it grows the overall pie,
15 both from a revenue perspective for Pandora, as well
16 as royalties to the copyright holders.

17 Q. Why has Pandora proposed to eliminate the
18 mechanical -- I'm sorry.

19 JUDGE FEDER: Excuse me.

20 THE WITNESS: The judge had a question.

21 JUDGE FEDER: This rate is going to be
22 about five years. Our next proceeding will be five
23 years from now.

24 What is the -- in your estimation being
25 in this business, are the offerings that are laid

1 out in the current rate structure likely to be the
2 same offerings that are out there in the marketplace
3 five years from now?

4 THE WITNESS: I hope -- I hope not
5 exclusively. I -- I think it lays good foundation
6 to grow the ecosystem of consumers paying for music
7 again. Having multiple price points is really
8 important for that, I -- I believe personally as a
9 businessman, running -- working in this industry.

10 What I would like to see over the next
11 five years is more diversity around offerings like
12 on this run, and we have those conversations with
13 our music industry partners constantly.

14 You know, in my -- this is my fourth
15 subscription business that I've launched. The other
16 three are very different industries, not
17 music-related. In every one, they were optimized by
18 creating multiple price points, multiple product
19 configurations, in order to meet different demands,
20 whether it was consumer or enterprise.

21 I think music has -- has been forced into
22 this one price, one product, all -- you know,
23 all-you-can-eat bucket for too long. The more we
24 can diversify that, the better it is for the
25 industry. I think the industry has started to

1 recognize that.

2 And if that continues, this is one step
3 in that direction, having two products at Pandora,
4 three. You know, I would foresee that we would have
5 multiple products in addition to those three by five
6 years from now.

7 JUDGE BARNETT: Would you foresee them
8 petitioning for another rate proceeding to set rates
9 for something that's totally different and outside
10 the categories in Subparts B and C?

11 THE WITNESS: I'm not sure how we would
12 pursue licensing, to be honest. You know, we -- we
13 would likely go and try and do direct deals
14 initially, for sure, in order to experiment. That
15 is really difficult because of the fractured nature
16 of the royalty structures, you know, and the
17 ownership, uncertainty, and all the issues that we
18 have, especially in the publishing world.

19 But, you know, that's one of the reasons
20 we've been working hard on identifying rights,
21 creating those databases, not just us, other
22 distributors in the marketplace, because having that
23 allows us to have the right conversations to -- to
24 bring different products to market. But whether
25 that turns into -- whether that can be enabled

1 through a rate proceeding or not is not my
2 expertise.

3 JUDGE BARNETT: For your non-interactive
4 and your custom and ad-supported prospective
5 Premium, all of those services rely on the Music
6 Genome Project, correct?

7 THE WITNESS: Correct.

8 JUDGE BARNETT: So if somebody is
9 listening for free, asks to listen to Imagine,
10 they're going to get the same song as they would if
11 they were in -- in the Premium pool and asked to
12 listened to Imagine? They're going to hear the same
13 song, correct?

14 THE WITNESS: Well, except that in the
15 free service, there is no on-demand functionality.
16 So you could seed a station with Imagine, but under
17 the DMCA restrictions, we couldn't just play
18 Imagine.

19 Now, if Imagine is played on that station
20 or a Beatles station or a cover of it is played by
21 -- Pentatonix just did an amazing version of it --
22 then, you know, you -- it would be the same song
23 that you would hear on the two services. So the --
24 the actual musical work that's played is the same
25 musical work, but what's different as you -- if you

1 were listening to it on Plus, you could listen to it
2 off-line in a subway when you had no connection,
3 where you couldn't in the free product.

4 If you're listening on Premium, you could
5 say I want to listen to Imagine and I want John
6 Lennon's version, not Pentatonix, and you could
7 choose a specific version besides what the genome
8 decided to play for you.

9 So the idea is you give that value
10 proposition of additional control, features, and
11 functionality to move people up that value chain in
12 order to drive higher ARPU for us, but also in
13 exchange for the features and functionality to be
14 licensed in those contexts, you know, it's a -- it
15 pays a higher royalty to the -- to copyright holders
16 as well.

17 JUDGE BARNETT: Okay. So -- but if a
18 subscriber pays \$4.99 --

19 THE WITNESS: Yes.

20 JUDGE BARNETT: -- or \$9.99 and they
21 request to listen to Imagine, they're going to hear
22 the same -- they want John Lennon's Imagine; they're
23 going to hear the same song?

24 THE WITNESS: They are, but the \$4.99
25 product is still radio. It's still -- they can't

1 put in Imagine and then hear the song. It's the
2 same concept of they could see the station or they
3 could put a Beatles station in and they could hear
4 Imagine if it's served, but they can't choose to --
5 to listen to that song.

6 JUDGE BARNETT: Okay.

7 THE WITNESS: So only by paying \$9.99 can
8 they actually do that piece.

9 JUDGE FEDER: To change the hypothetical
10 a little bit --

11 THE WITNESS: Sorry.

12 JUDGE FEDER: -- if the \$4.99 customer
13 were to seed a station with Imagine and the \$9.99
14 customer were to start a playlist with Imagine, are
15 they going to end up with the same list of songs
16 either on the radio side -- not necessarily in the
17 same order, but on the radio side and on the
18 generated playlist using the music genome?

19 THE WITNESS: It's the same user, if it's
20 you?

21 JUDGE FEDER: Um-hum.

22 THE WITNESS: Yeah, it likely would be
23 the same or very, very similar playlist because we
24 would use your musical preferences as determined by
25 your demographics, your geographics, the music you'd

1 be listening to, what you've thumbed up. So -- so
2 for you, yes.

3 But for Ben, you know, he likes the
4 Beatles, but he likes a different -- he's a Sergeant
5 Pepper guy where you're a Rubber Soul guy, right?
6 So you could -- he'll hear a different mix in both
7 cases, but from a between products, it would be the
8 same sort of data that's used to create that
9 playlist, whether it's a radio station in Plus or a
10 -- or adding similar songs feature within Premium.

11 The difference in Premium now is you can
12 -- you see all the songs that are going to play. In
13 Plus, you don't get to know. It just plays for you.
14 And you can say, yeah, not that one, not that one,
15 not that one, and reorder them. So functionality
16 that's very specific to on-demand listening, that
17 will exist in Premium; none of that exists in Plus.

18 BY MR. MARKS:

19 Q. Just so the record is clear, you used the
20 interpret ARPU. What is ARPU a reference to?

21 A. ARPU is average revenue per user.
22 Usually referred to as average annual revenue per
23 user, although you can get a month. Sometimes it's
24 monthly; sometimes it's less. So if we talk about
25 the ARPU of a Premium user, at 9.99, it's

1 approximately \$120 per year.

2 Q. Why has Pandora proposed to eliminate the
3 mechanical-only floor in Subpart B?

4 A. Well, this goes back to, you know, what I
5 -- you know, the difference -- the distinction
6 between mechanical and performance from a business
7 perspective is not -- is not a meaningful one. So,
8 you know, there might be a purpose for that that I
9 don't -- you know, that I'm not aware of or that
10 doesn't matter to me, but from my purposes, it adds
11 complexity into a system that's not needed. I'd
12 rather just have a single rate and a single
13 calculation.

14 Q. Why has Pandora proposed to adjust the
15 terms of the current regulations to accommodate
16 promotional efforts such as family plans and student
17 discounts?

18 A. Yeah, so this actually goes back a little
19 bit to the price diversity conversation we were
20 having earlier about \$4.99 to \$9.99. By creating
21 different price points, you access users that
22 wouldn't otherwise subscribe.

23 So students who have a smaller budget, as
24 long as they are still students, having a student
25 plan that is at a discount, it allows them to be a

1 paying customer, teaches them about paying for
2 music, builds that habit, and then when they
3 graduate and enter the workforce or, you know,
4 society generally, then they upgrade, you know, more
5 -- more naturally into being -- paying a standard
6 price.

7 Similar with family plans, you know, you
8 have children in the -- in the home that are not
9 necessarily going to have their own subscription, we
10 can get -- add to the overall revenue pie, also
11 engage with listeners at a younger age or an older
12 age. We actually see family plans used for
13 grandparents and such as much as we see it used for
14 kids. People who we can add to the subscription
15 roles who wouldn't necessarily do their own
16 subscription.

17 Now, the -- a side benefit of that is
18 we're monetizing an audience that's extremely hard
19 to monetize in an ad environment. So, you know,
20 from a business perspective, you get two benefits.
21 You get the benefit of -- of monetizing in a
22 subscription environment an audience that would
23 otherwise not subscribe. So you're adding
24 incremental subscribers to the pool. That's good.

25 Second is you're targeting those

1 incremental subscribers out of pools that are hard
2 to monetize anyway, 13- to 17-year-olds, really hard
3 to monetize with advertising; 55 and older, really
4 hard to monetize from advertising. So those are two
5 pools that, if we can convert as many of them as we
6 can in subscription, that's good for both us as a
7 business, but also for copyright holders as it
8 increases their overall royalty payments.

9 Q. Have you reviewed the Copyright Owners'
10 rate proposal in this proceeding?

11 A. Yes.

12 Q. Let me show you a slide with a few
13 aspects of the Copyright Owners' rate proposal
14 depicted and ask you to comment on some of them.

15 Why is Pandora opposed to the imposition
16 of a per-play minimum rate in this proceeding?

17 A. Well, you know, it's connected to why I
18 think percentage of revenue makes sense. A per-play
19 consumption-based model where the revenue is fixed
20 per user creates a lot of -- of uncertainty and
21 volatility around what margins are going to be for
22 that product. That's a business problem. And, you
23 know, from a business perspective, that uncertainty
24 means that I'll less invest less in that business,
25 you know, that I -- I don't know how much I'm going

1 to make over time. So there's that aspect of it.

2 Second is it's a perverse incentive for
3 me to limit listening in a subscription --
4 subscriber environment. And that's not -- that's
5 not in anybody's interest who is getting paid out of
6 a subscription basis, whether it's us or the
7 copyright holders. So engagement, or the number of
8 hours -- we measure engagement by hours per user per
9 month -- is the Number 1 indicator as to whether
10 someone will convert from a trial into subscription
11 or continue to subscribe, retain over time or churn
12 out.

13 And if -- if we're paying on a per-play
14 basis, we have an incentive to reduce listening as
15 much as possible in order to be profitable. By
16 reducing engagement, we increase the propensity to
17 churn or likelihood to cancel.

18 And that -- that is -- now I've got two
19 incentives that fight against each other. Of
20 course, I don't want them to cancel, but I also
21 can't afford them if the per-play rate is -- it
22 doesn't work in the -- in the context of what
23 revenue I can charge.

24 JUDGE STRICKLER: Why would the per-play
25 rate cause an increase in churn?

1 THE WITNESS: Because it's -- there's a
2 step in the middle. So if there's a per-play rate,
3 my incentive is to reduce the hours people consume
4 of music. So if I do that, it lowers engagement.
5 Engagement is the Number 1 indicator as to retention
6 over time or the -- which is the opposite of churn.

7 So there's a direct correlation between
8 engagement or hours per use, hours per user, and --
9 and churn. So the higher hour per user, the lower
10 churn. If I'm incentivized to hold hours per user
11 down, churn is going to go up. That is a -- that is
12 a truism among subscription businesses. All four
13 that I've run, that's been the truth.

14 To be honest, one of the reasons why we
15 focused on percent of revenue in all our sound
16 recording deals, the direct deals, is that, you
17 know, that argument was completely adopted by the
18 labels in the context of what they want is build
19 subscribers who stay subscribers for a long time,
20 right?

21 And we've aligned -- when we say win/win,
22 it's we're aligned to the royalty structure to the
23 business objective of Pandora and the -- and the
24 long-term royalty streams of the copyright holders
25 in that environment.

1 That's what we're trying to accomplish
2 by percent of revenue in this case. A per-play
3 structure blows that up.

4 JUDGE BARNETT: Mr. Herring, if you have
5 a subscription service and if the royalty rate is a
6 per-play rate and it's low enough that it would
7 essentially equal what you're paying on a percent of
8 revenue, then why would you discourage listening
9 and, therefore, discourage engagement and,
10 therefore, you know, encourage churn?

11 THE WITNESS: Well, low enough is a very
12 important --

13 JUDGE BARNETT: Okay. I got that.

14 THE WITNESS: -- qualifier there. So, I
15 mean --

16 JUDGE BARNETT: What --

17 THE WITNESS: If you remember, in the --
18 in the last time I was in front of you, there was a
19 per-play rate under subscription in that
20 environment. And it was about 70 hours, was the
21 break-even. If you listen to more than 70 hours a
22 month at that rate, I have now lost money on every
23 subscriber. And so we -- we, you know, would find
24 ways to hold back listening.

25 So if that rate was really, really,

1 really minuscule so that it never broke through a
2 percentage of revenue number, then it becomes
3 irrelevant, but that's -- the risk is that that rate
4 is too high, and that it creates problem --
5 unintended consequences based on engagement.

6 And Pandora has -- you know, maybe we're
7 more sensitive because our engagement is much higher
8 than anybody else in the industry.

9 JUDGE BARNETT: Just in what ways would
10 you discourage listening, if it were a per-play
11 rate? And wouldn't you be doing that -- that's
12 cutting off your nose to spite your face because
13 you're going to lose a subscriber if you do that?

14 THE WITNESS: Can we go into restricted
15 session? This -- I mean, this is kind of --

16 MR. MARKS: Can we go in restricted
17 session?

18 JUDGE BARNETT: Were you planning to do
19 that later?

20 MR. MARKS: We are.

21 JUDGE BARNETT: Okay. Well --

22 THE WITNESS: Could I answer that
23 question --

24 JUDGE BARNETT: Yes, please.

25 THE WITNESS: -- without my competitors

1 in the room?

2 JUDGE BARNETT: You may.

3 THE WITNESS: Thank you.

4 JUDGE STRICKLER: I think they're getting
5 up now.

6 JUDGE BARNETT: No, we're not -- we're
7 not going into restricted yet.

8 THE WITNESS: We're not yet. Sorry.

9 BY MR. MARKS:

10 Q. We'll go into restricted fairly shortly
11 so we can come back to it.

12 What is your view of the Copyright
13 Owners' proposal to charge a per-play rate to all
14 streams that are made in connection with a product
15 that offers both interactive features and
16 non-interactive listening within the same product?

17 A. Yeah, I -- I mentioned earlier, we expect
18 non-interactive listening to be 70 percent or more
19 of listening in the interactive product, in the
20 product that offers interactive listening. So, I
21 mean, applying a per-play rate across is meaning
22 paying a much higher rate on streams that aren't --
23 you know, aren't enabled by that licensing.

24 Q. Is the Copyright Owners' proposal to
25 apply a single rate to the entire marketplace for

1 services with interactive features a good idea?

2 A. No.

3 Q. Why not?

4 A. It essentially eliminates the ability to
5 price differentiate a \$4.99 versus a \$9.99 product.
6 So I think it's really important to keep that
7 structure that allows us to have some diversity in
8 product.

9 JUDGE STRICKLER: I don't know if you can
10 answer this without going into restricted session,
11 but building on Judge Barnett's question from
12 before, has Pandora considered a hybrid approach or
13 what economists would say is a two-part tariff,
14 where you have a certain monthly subscription fee
15 but then there's a small per-play rate as well
16 because you just testified before about the essence
17 of the problem is getting a per-play -- a per-play
18 rate that's low enough --

19 THE WITNESS: Yeah.

20 JUDGE STRICKLER: -- that it makes sense.
21 And -- and that's the risk that you take. If you
22 get it wrong, then you might have to have listener
23 caps or other ways to dissuade listening.

24 THE WITNESS: Yeah.

25 JUDGE STRICKLER: But can you sort of

1 have your cake and eat it too with the two-part
2 tariff, setting a low -- a very -- well, a given
3 subscription rate lower than the \$9.99 or lower than
4 the \$4.99 and then have usage rates, per-play rates,
5 that are sufficient --

6 THE WITNESS: Yeah.

7 JUDGE STRICKLER: -- to be able to make a
8 profit?

9 THE WITNESS: So, yes. That's been
10 something that has been debated pretty intently.
11 You know, we're trying to learn from mistakes of the
12 past. So if you think about cell phone plans have
13 made that migration already.

14 JUDGE STRICKLER: Right.

15 THE WITNESS: The issue is twofold. The
16 one is that type of structure is -- is complex to --
17 it does come out of the complexity. So complex to
18 manage from our perspective in terms of managing 80
19 million individual accounts and what they're paying
20 us and what they're not.

21 On a per-song basis, we're talking about
22 fractions of pennies, so until Bitcoin is really
23 widely adopted, that's going to be difficult.

24 But even if you did buckets and you based
25 it on hours, that would get -- it just gets

1 complicated really quickly. So, administratively,
2 that's really hard.

3 Now, more importantly -- not impossible,
4 but hard. More importantly, it's consumer
5 confusion, and -- and adoption is really the
6 problem. And the perception in value.

7 And the reality is the focus on this for
8 a few users ignores the fact that most -- most users
9 are -- you know, in that example I gave you where
10 the break-even is at 70, that was 1.2 percent of our
11 subscribers were unprofitable, you know. So we do
12 deal with it in the context of a -- because the rate
13 was low enough, to use your -- your term.

14 But that, as a -- as a consumer value
15 proposition, is really hard to do. There's this --
16 there's this view that even if people never are
17 going to hit that sort of threshold, the threat that
18 they're going to have to write a variable check
19 every month is enough for people not to subscribe.
20 And when we did our own analysis as to how big --
21 you know, how we can market this, how it can be
22 competitive against other services and such, adding
23 complexity into the consumer experience is a big red
24 flag.

25 So there's both administratively and

1 incredibly difficult. You know, a couple more tens
2 of millions of dollars in development costs, but,
3 you know, which we don't have. And then the other
4 side of it is and for a lower return. So you're --
5 you're kind of killing me on both ends.

6 BY MR. MARKS:

7 Q. Do you think the Copyright Owners'
8 proposal to impose a late fee on mechanical rights
9 payments is reasonable?

10 A. No.

11 Q. Why not?

12 A. Well, I mentioned earlier the fractured
13 nature of ownership here is really difficult. We
14 pay everybody we can figure out to pay and we pay
15 them on time. We don't play games on that front at
16 all. Ownership can be complex on a down-to-the-song
17 level. It's certainly complex on an industry level
18 in terms of it changes a lot.

19 There's no single repository. The
20 metadata is incomplete and something that we will
21 work very hard internally to get right. We've spent
22 substantial sums to a third party to help us solve
23 these problems. So we -- we make every effort to do
24 this the right way, but -- and we pay every dollar
25 we can -- we can pay. And always have.

1 So I don't -- I think it's a solution in
2 search of a problem that doesn't exist. The real
3 problem is the data issues, and incentive to get
4 that data right is important, i.e., incentive to get
5 paid.

6 And if you add a license fee or, sorry, a
7 late fee and, God forbid, a user's late fee on top
8 of that, the incentive to get that data right soon
9 lessens significantly. And already we -- I think we
10 have a hard time getting data accurate to make the
11 payments that we want to make.

12 I think adding a late fee just creates
13 the wrong environment between us and our publishing
14 partners.

15 Q. For works for which Pandora does not have
16 reliable ownership information at the end of a
17 royalty accounting period, would Pandora be opposed
18 to putting royalty payments in an interest-bearing
19 escrow account until publishers or the NMPA could
20 provide reliable ownership information?

21 A. No.

22 JUDGE STRICKLER: No, you would not be
23 averse?

24 THE WITNESS: No, I would not be averse
25 to that.

1 MR. MARKS: At this point, Your Honors,
2 if we could clear the courtroom, we're going to go
3 into restricted session.

4 JUDGE BARNETT: Okay. Now we're closing
5 the hearing room. If you are in the hearing room
6 and do not have privilege to hear or see restricted
7 materials, if you would please wait outside.

8 (Whereupon, the trial proceeded in
9 confidential session.)

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1 O P E N S E S S I O N

2 BY MR. MARKS:

3 Q. I should say, in the interest of full
4 disclosure, a few short topics, not just a few
5 questions.

6 THE WITNESS: Break out my long answers.
7 Use up the time. We're ready.

8 JUDGE BARNETT: Yes.

9 BY MR. MARKS:

10 Q. Mr. Herring, what is Ticketfly?

11 A. It is a software and service ticketing
12 platform that -- that venues use to sell advanced
13 tickets.

14 Q. Could you turn to the tab in your binder
15 that's marked Pandora Exhibit 892?

16 A. Yes.

17 Q. What is it?

18 A. This is a description of the company from
19 their web site.

20 Q. When you say "company," you're referring
21 to --

22 A. Ticketfly.

23 Q. Was this document appended to your
24 written rebuttal testimony as an exhibit?

25 A. Yes.

1 MR. MARKS: I offer Pandora Exhibit 892
2 into evidence.

3 MS. BUCKLEY: No objection.

4 JUDGE BARNETT: 892 is admitted.

5 (Pandora Exhibit Number 892 was marked
6 and received into evidence.)

7 BY MR. MARKS:

8 Q. Does Ticketfly utilize mechanical rights
9 to musical works?

10 A. No.

11 Q. How does Ticketfly generate revenue?

12 A. It takes a fee on a per-ticket basis for
13 every ticket sold through its platform.

14 Q. Can a Pandora user purchase a concert
15 ticket through Ticketfly on Pandora's web site or
16 app?

17 A. No.

18 Q. Do you need to be a Pandora user in order
19 to buy tickets to a concert through Ticketfly?

20 A. No.

21 Q. Does Pandora offer alerts about upcoming
22 concerts held at venues other than the ones that use
23 Ticketfly to sell tickets?

24 A. Yes.

25 JUDGE STRICKLER: Question for you. On

1 Exhibit 892, it says Ticketfly is a subsidiary of
2 Pandora. Is it a wholly-owned subsidiary?

3 THE WITNESS: It is.

4 BY MR. MARKS:

5 Q. Does Pandora receive any commission fee
6 if a Pandora user buys a -- buys concert tickets
7 through the link provided in Pandora's streaming
8 service?

9 A. No.

10 Q. Is Ticketfly operated as a separate
11 business from Pandora?

12 A. Yes.

13 Q. Does it have separate P&L statement?

14 A. It does.

15 Q. Does it have any overlap in management
16 teams?

17 A. No, it has its own management team.

18 Q. What percentage of Pandora's consolidated
19 revenues come from Ticketfly?

20 A. About 6 percent.

21 Q. And has Pandora done projections of what
22 percentage of consolidated revenues Ticketfly will
23 represent going into the future?

24 A. Approximately the same, maybe growing a
25 little bit to 7 percent.

1 Q. Can Pandora operate as an unprofitable
2 music service because of its ownership of Ticketfly?

3 A. No.

4 Q. Has Pandora ever offered its music
5 streaming service at a discount or for free to drive
6 customers to Ticketfly?

7 A. No.

8 Q. Does Pandora have any incentive to
9 operate its music streaming products at a loss?

10 A. No.

11 Q. Do any of Pandora's licenses with record
12 labels, performing rights organizations, or music
13 publishers include, for purposes of calculating a
14 fee, Ticketfly revenues within the definition of
15 Pandora's revenue?

16 A. No.

17 Q. Do songwriters and music publishers
18 benefit financially if Pandora drives incremental
19 concert ticket sales by alerting its users about
20 concerts?

21 A. Yes.

22 Q. How?

23 A. The venues that Ticketfly sells tickets
24 for and -- and the venues that we don't sell tickets
25 for that we drive tickets for pay performance fees

1 to ASCAP, BMI, SESAC, et cetera, so that songwriters
2 and publishers receive royalties in that way.

3 Q. If you could turn to the tabs that are
4 marked as Pandora Exhibits 893, 894, and 895.

5 A. Yes.

6 Q. Do you recognize these documents?

7 A. Yes.

8 Q. What are they?

9 A. These are performance agreements for
10 ASCAP, BMI, for live events venues.

11 Q. Are you personally familiar with these
12 documents?

13 A. Yes.

14 MR. MARKS: I offer Pandora Exhibits 893,
15 894, and 895 into evidence.

16 MS. BUCKLEY: I -- I object. The mere
17 fact that Mr. Herring may be familiar with this
18 document is not the same thing as saying that he
19 uses it in Pandora's business or that he licenses
20 anything pursuant to these agreements.

21 BY MR. MARKS:

22 Q. Mr. Herring, have you -- have you ever
23 entered into a -- an agreement of this nature?

24 A. Well, we do put on live events where we
25 have licenses like of this nature. I also own a

1 live event venue that is licensed with ASCAP, BMI,
2 and SESAC using these agreements.

3 MS. BUCKLEY: I don't think agreements of
4 this nature is the same thing as saying that Pandora
5 has entered into any of these agreements.

6 MR. MARKS: We're not representing
7 Pandora has entered into these specific agreements.
8 We're representing that these are the form
9 agreements that ASCAP and BMI use to license concert
10 venues and concert promoters to provide further
11 evidence that additional ticket sales drives
12 additional revenues to rightsholders.

13 JUDGE BARNETT: Sustained. 894, 895, 897
14 -- are those the numbers?

15 MR. MARKS: I think it's 893, 894, and
16 895.

17 JUDGE BARNETT: That's right. Thank you.
18 Are rejected.

19 (Pandora Exhibits 893, 894, 895 were
20 rejected from evidence.)

21 BY MR. MARKS:

22 Q. Does Pandora have any concerns that there
23 will be less musical works available in the future
24 for Pandora to stream and make available to
25 consumers if Pandora's rate proposal is adopted?

1 A. No.

2 Q. Why not?

3 A. There has been no shortage of music
4 available over the last few years under these rates.
5 ASCAP, BMI continue to grow and add works to their
6 repertoire, which we're licensed with.

7 We have done multiple direct deals in
8 that same time frame.

9 Q. What is your familiarity with the growth
10 of repertory of ASCAP and BMI?

11 A. Well --

12 MS. BUCKLEY: Objection. Unless it's
13 based on personal knowledge, I don't think that this
14 is appropriate testimony for this witness. If all
15 he has done is read ASCAP's annual report, which is
16 pure hearsay, I really don't think he can talk about
17 what is happening at ASCAP in terms of how many
18 writers there are.

19 JUDGE BARNETT: I got -- I got the
20 objection.

21 MS. BUCKLEY: Thank you.

22 JUDGE BARNETT: Do you want to try and --

23 MR. MARKS: Yeah, but the question I
24 asked him was what is his familiarity with the
25 growth, and I think he should be allowed to answer

1 and explain so I can lay a foundation.

2 JUDGE BARNETT: Okay.

3 THE WITNESS: You know, we are partners.

4 We have deals, and have for years, with ASCAP and
5 BMI, and I read their annual reports and their own
6 statements about their repertoire.

7 BY MR. MARKS:

8 Q. And do you consider the size of the
9 repertoire, the growth of the repertoire as you --
10 in evaluating performance rights licenses?

11 A. Yes, they are directly connected to our
12 negotiations for licensing.

13 Q. If I could turn your attention to Pandora
14 Exhibits 897 through 902. I'll ask you if you
15 recognize these documents?

16 A. Yes, these are the --

17 MS. BUCKLEY: I object to these exhibits
18 on the same basis.

19 JUDGE BARNETT: They haven't been offered
20 yet.

21 MS. BUCKLEY: Okay.

22 BY MR. MARKS:

23 Q. What are the -- what are the documents
24 that have been included in your binder as Pandora
25 Exhibits 897 to 902?

1 A. They are the annual reports for ASCAP,
2 for 2013, '14, and '15, and then for BMI, 2013,
3 2014, and 2015.

4 Q. And did you receive these documents in
5 the ordinary course of business?

6 A. Yes.

7 Q. Did you also review these documents in
8 preparation for your -- in preparing your written
9 rebuttal testimony?

10 A. Yes.

11 Q. Were they attached as exhibits to your
12 written rebuttal testimony?

13 A. Yes.

14 Q. Are these available to the public on
15 ASCAP and BMI's web site?

16 A. Yes.

17 MR. MARKS: Your Honors, I'd like to
18 offer Pandora Exhibits 897, 898, 899, 900, 901, and
19 902.

20 MS. BUCKLEY: Objection, there's no
21 foundation for these hearsay documents.

22 JUDGE BARNETT: Are you offering these
23 for the truth of the matter?

24 MR. MARKS: No, I'm offering them as --
25 as informing Pandora's testimony, Mr. Herring's

1 testimony, about whether or not there's any concern
2 from the Service perspective about whether or not
3 there won't be enough musical works available to
4 operate his service.

5 MS. BUCKLEY: Objection. It sounds like
6 what he just said is that Mr. Herring is going to be
7 relying on these documents for which -- which are
8 hearsay for which there's no foundation, to support
9 his claim that there's no shortage of writers.

10 MR. MARKS: I'd also like to respond that
11 ASCAP and BMI are organizations that represent music
12 publishers and songwriters. I think it's an
13 admission against interest. They're owned by the
14 same people that the Copyright Owners here purport
15 to represent. So these are the annual reports that
16 are publicly available, widely distributed to
17 licensees and other content partners. Frankly, I'm
18 surprised that they want to deny what the numbers
19 say.

20 JUDGE BARNETT: The objection is
21 overruled. These are being admitted not to support
22 the truth of what ASCAP and BMI say their financials
23 are or their -- whatever. They're just being
24 offered as -- as materials upon which Mr. Herring
25 relies in his business decision making. Whether

1 they're --

2 MS. BUCKLEY: As long as they're not
3 being relied on for the truth of the contents.
4 Thank you.

5 JUDGE BARNETT: I don't see how we could
6 do that. So --

7 MR. MARKS: Thank you, Your Honors. No
8 further questions.

9 JUDGE BARNETT: Yes. Oh, I'm sorry.

10 MR. MARKS: I'm sorry. Before I yield
11 the microphone --

12 JUDGE BARNETT: Did we start with 897?
13 897 through 902 inclusive are admitted.

14 (Pandora Exhibit Numbers 897, 898, 899,
15 900, 901, and 902 were marked and received into
16 evidence.)

17 MR. MARKS: Thank you, Your Honors. No
18 further questions.

19 JUDGE BARNETT: Let's have a 20-minute
20 recess. I'm not sure where everyone stands on
21 having missed their lunch or eaten their lunch or
22 taken an early lunch or if you want a snack. So
23 we'll take 20 minutes, which will get us to about 8
24 -- or, sorry, 2 -- let's just say 2:10 and call it
25 good.

1 (A recess was taken at 1:48 p.m., after
2 which the hearing resumed at 2:18 p.m.)

3 JUDGE BARNETT: I anticipate some
4 cross-examination of Mr. Herring, but he chose not
5 to come.

6 (Laughter)

7 JUDGE BARNETT: Thank you, Mr. Herring.
8 You may remain under oath. Are we in open session?

9 MS. BUCKLEY: I think very briefly, and
10 even then it's simply based on the fact that there
11 were certain material in Mr. Phillips' testimony
12 that was not designated as restricted, and I'm going
13 to go over some of that, but if counsel believes
14 otherwise, I'm happy to treat it as restricted.

15 JUDGE BARNETT: Okay. All right. Thank
16 you.

17 CROSS-EXAMINATION

18 BY MS. BUCKLEY:

19 Q. Good afternoon, Mr. Herring.

20 A. Hi.

21 JUDGE BARNETT: Ms. Buckley, could you
22 identify yourself for the record and lower that mike
23 just a little bit so it picks up your voice?
24 Thanks.

25 MS. BUCKLEY: My name is Lisa Buckley.

1 I'm from Pryor Cashman and represent the Copyright
2 Owners.

3 BY MS. BUCKLEY:

4 Q. Mr. Herring, you spend a significant
5 portion of your written direct testimony and also
6 your testimony this morning talking about the Music
7 Genome Project. Do you recall that?

8 A. Yes.

9 Q. And you talked about the expense
10 associated with creating it and the time and effort
11 that it took to create it. These are all expenses
12 and time that would have been spent and incurred
13 regardless of whether Pandora expanded its service
14 into Plus and Premium; isn't that correct?

15 A. Yes.

16 Q. And just to be clear, the Music Genome
17 Project was not something that Pandora created in
18 connection with its decision to expand its service
19 offerings to Plus and Premium, correct?

20 A. Yes.

21 Q. And Pandora would continue to update the
22 Music Genome Project regardless of whether it had
23 made the decision to expand its service offerings
24 from purely a non-interactive service, correct?

25 A. Not at the same level, but that activity

1 would probably -- the breadth of coverage necessary
2 under interactive service is dramatically more than
3 a radio service.

4 Q. Does that -- when you refer to that, are
5 you referring to breaking down additional songs
6 through the Music Genome Project?

7 A. Yes.

8 Q. And what -- what would be the difference,
9 if you will, between what you would do if you just
10 maintained your non-interactive service as opposed
11 to what you would do in connection with your
12 additional service offerings?

13 A. So in a non-interactive service, we
14 choose the song that we play for you. And
15 99 percent of the songs that people want to hear in
16 that environment are contained within a catalogue of
17 maybe a couple million.

18 In an on-demand environment, the value
19 proposition is different. Although as I stated
20 earlier today we believe north of 70 percent of
21 listening will still be in a non-interactive
22 environment, the remaining piece, which is a big
23 part of why people are paying for the subscription,
24 the value proposition, is that they can hear a
25 specific song when they enter it. And so the need

1 for a much broader catalogue is important because
2 the value proposition is if you want to hear a
3 specific song, you enter it.

4 And so instead of a couple million songs
5 being sufficient to power the service, you know, it
6 is tens of millions of songs.

7 Q. And in addition to the Music Genome
8 Project, Pandora also breaks songs down by
9 algorithm, correct?

10 A. Not -- we use machine learning to
11 evaluate songs, yes, in connection with human
12 analysis through the genome project.

13 Q. The Premium service, I believe you said,
14 is launching tomorrow?

15 A. In limited release, yes.

16 Q. Congratulations.

17 A. Thank you.

18 Q. Has Pandora analyzed through the Music
19 Genome Project the number of songs in its on-demand
20 library?

21 A. Not every song in the on-demand library.
22 That's not the way it works.

23 Q. How many songs are in the on-demand
24 library?

25 A. Can we go into restricted session?

1 Q. Yes.

2 A. You're now asking me questions that are
3 not public.

4 JUDGE BARNETT: Thank you.

5 (Whereupon, the trial proceeded in
6 confidential session.)

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1 C O N T E N T S

2 WITNESS DIRECT CROSS REDIRECT RECROSS

3 MICHAEL HERRING

4 842 936 1037 1052

5

6 CONFIDENTIAL SESSIONS: 906-924, 941-end

7

8 E X H I B I T S

9 EXHIBIT NO: MARKED/RECEIVED REJECTED

10 PANDORA

11 880 845

12 881 850

13 882 873

14 888 845

15 889 910

16 891 866

17 892 926

18 893 930

19 894 930

20 895 930

21 897 935

22 898 935

23 899 935

24 900 935

25 901 935

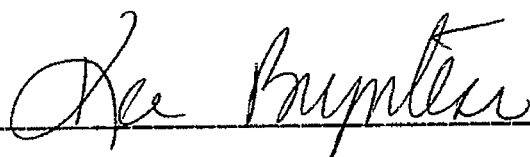
1	EXHIBIT NO:	MARKED/RECEIVED	REJECTED
2	PANDORA		
3	902	935	
4	905	979	
5	974	908	
6	COPYRIGHT OWNERS		
7	2694	958	
8	2746	973	
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CERTIFICATE

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I certify that the foregoing is a true and
accurate transcript, to the best of my skill and
ability, from my stenographic notes of this
proceeding.

3/15/17



Signature of the Court Reporter